Annual Report 1987/1988

British Columbia Petroleum Corporation

88-05585/

British Columbia Petroleum Corporation

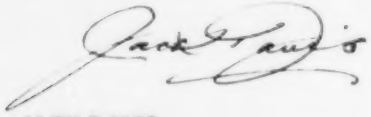
BC
B71
B
761-88
2

LETTER OF TRANSMITTAL

To His Honour the Honourable
Robert G. Rogers,
Lieutenant-Governor of the
Province of British Columbia

MAY IT PLEASE
YOUR HONOUR:

I have the pleasure to submit the Annual Report of the British Columbia Petroleum Corporation for the year ended March 31, 1988.



JACK DAVIS,
Minister of Energy,
Mines & Petroleum Resources,
Province of British Columbia

THE CORPORATION

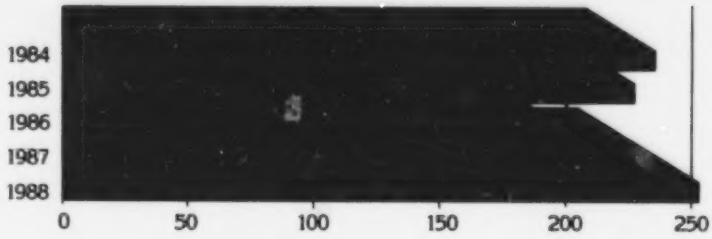
The British Columbia Petroleum Corporation was established on November 8, 1973, as an agency of the Crown, under the Petroleum Corporation Act. The primary function of the Corporation is to market natural gas produced in British Columbia by purchasing gas from producers and selling it to Westcoast Energy Inc., under an agreement dated November 13, 1973.

Under this agreement, Westcoast Energy Inc. novated all its British Columbia gas purchase contracts to the Corporation while retaining the functions of gathering, processing and transporting the gas and selling it to the various domestic utilities and to its U.S. customer, Northwest Pipeline Corporation. Westcoast retains from the proceeds of gas sales its cost of service, including a return on its rate base, and remits the balance of the proceeds to the Corporation, which in turn deducts its cost of service and distributes the remainder to the producers in accordance with the Natural Gas Price Act. Under the natural gas marketing system, which was implemented on July 1, 1985, the producers pay a royalty on the revenues that they receive from the sale of gas and by-products and therefore no revenues from the resale accrue to the Corporation.

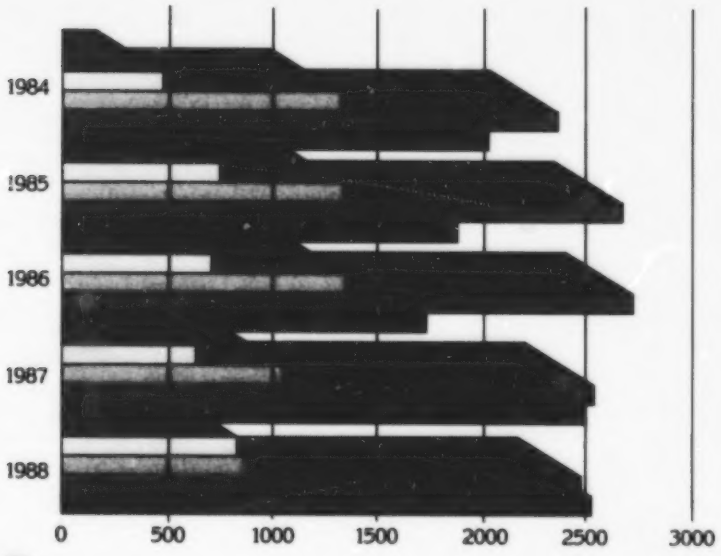
Report of the Directors

Sales of gas during the year under review declined by 4.4% to 6,350 from 6,642 million cubic metres, but the figures do not reflect the substantial changes that occurred in our export market. For most of the year sales to the Pacific Northwest and California were running strongly ahead of the previous year, and, as late as this January, it was still reasonable to expect another satisfactory year. However, on February 10 Northwest Pipeline Corporation, until then the principal buyer of the Corporation's gas, offered to provide open access transportation service, thus conceding to their local distribution companies and their customers the ability to buy gas from other sources. The resulting competition for sales was, and is, intense and widespread, and as a consequence, the Corporation's sales suffered a severe decline as did the prices it received for the gas. This condition is expected to continue, at least in the near term, until Northwest Pipeline adopts open access under FERC Order 500.

Natural Gas Liquids Sales (thousands of cubic metres)



Natural Gas Sales (millions of cubic metres)



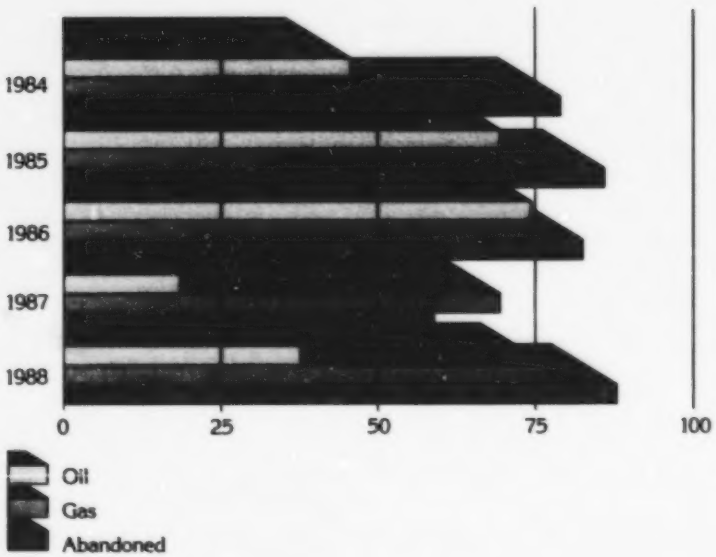
Pacific Northern Gas Ltd.
Inland Natural Gas Company Ltd.
British Columbia Hydro and Power Authority
Exports of British Columbia Gas

Sales to our domestic market declined by 8% reflecting the further loss of part of the B.C. industrial sector to short-term direct sales.

Most of the export sales made by the Corporation take place under a contract that exists between Northwest Pipeline and Westcoast Energy Inc. During the year significant amendments were made to this contract which had the effect of resolving a dispute concerning the collection of tolls and, more importantly, introduced a method of cost recovery for the gathering, processing, and transmission of gas that enabled the Corporation to increase the price it pays for the gas it buys.

Sales of natural gas liquids increased by 9.5% and, with some improvement in prices over the previous year, the Corporation's revenue from this

Wells Completed (by classification)



source increased by 26%. Sales of sulphur were also higher and posted a gain of 12% in volume but, because of lower prices and the strength of the Canadian dollar, revenues declined by 29%.

The ongoing process of deregulation of the natural gas industry throughout North America has created some turmoil but has also caused the industry to re-examine its goals. As governments and regulators in both Canada and the United States ease their control over various segments of the industry there are opportunities created for the marketing of natural gas.

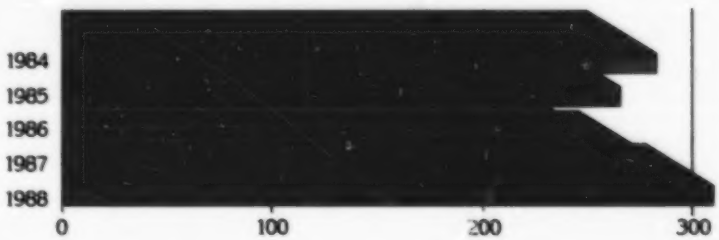
In keeping with this trend toward deregulation the Government of British Columbia has taken the initiative in opening up the natural gas industry to direct sales in the province and improved access to markets through less government involvement.

During the year the Government announced that it was examining the prospect of privatizing the marketing activities of the Corporation. A three man committee of the Board of Directors was appointed to examine and assess proposals that were received with respect to the privatization. Following recommendations made to the Board, the Government will determine when and how the Corporation's marketing function can be transferred to the private sector.

In conclusion, the Board would like to thank the staff of the Corporation for their efforts and support during this past year which was both trying and yet rewarding.

JACK DAVIS,
Chairman

Sulphur Sales (thousands of metric tonnes/shipped)



Natural Gas Prices

Under the Natural Gas Price Act, the Minister of Energy, Mines and Petroleum Resources is empowered to set a price, identified as the Producer Selling Price, at which the Corporation purchases natural gas under its contracts with producers, or acquires gas from a producer under an acquisition order. The Corporation may also, by order, establish a Price Adjustment for gas it acquires under a gas contract or an acquisition order. The Price Adjustment is calculated based on the balance of funds remaining in the Natural Gas Price Adjustment Fund after certain costs have been paid as set out in the Natural Gas Price Act. The total of the Producer Selling Price and the Price Adjustment equals the Regulated Selling Price.

The prices paid for gas purchased by the Corporation during the year are shown below:

	General Producer Selling Price $/10^3m^3$	General Price Adjustment $/10^3m^3$
1987		
April	47.7588	2.5402
May-Dec. . . .	44.9902	2.5402
1988		
Jan.-March . .	53.6422	2.0765

Financial Review

Under the natural gas marketing system which was established by the Natural Gas Price Act on July 1, 1985, the revenues received by the Corporation on the resale of gas and by-products are paid into the Natural Gas Price Adjustment Fund. Payments out of the fund comprise the Corporation's operating expenses and the Producer Selling Prices and Price Adjustments. In this manner, after the payment of the Corporation's cost-of-service, all revenues are flowed back to the producers.

The Corporation continues to administer the Petroleum Corporation Fund which reflects the transactions that occurred prior to July 1, 1985, and those transactions which are not governed by the Natural Gas Price Act.

The total volume of gas sold during the year amounted to 6,350 million cubic metres compared with 6,642 million cubic metres in the previous year. This reduction was primarily caused by the loss of sales in the domestic market to direct contracts, where the volume of gas sold declined from 4,146 million cubic metres to 3,822 million cubic metres. In the export market, the volume of gas sold increased slightly from 2,496 million cubic metres to 2,528 million cubic metres. Sales to the export market were affected by Northwest Pipeline Corporation ("NWP"), the major U.S. customer of Westcoast Energy Inc. ("Westcoast"), offering a form of open access transportation service on February 10, 1988. This

enabled NWP's customers to purchase gas directly from other suppliers and, as a result, a variety of marketers, including producers and brokers, entered into direct sales with those customers under negotiated short term contracts and captured sales that would otherwise have been made through the Corporation under the Westcoast/NWP sales contract.

Effective November 1, 1987, the price for gas purchased by the three major British Columbia utilities was renegotiated for the contract year commencing on that date. In addition, the Westcoast/NWP sales contract, which terminates on October 31, 1989, was amended to include, inter alia, a reduction to the contract demand and a revision to the allocation of fixed costs in the demand charge. These changes enabled the Corporation to increase, effective January 1, 1988, the price paid for gas purchased from producers. This price, which is shown in the table above, is not significantly different from the price paid by the Corporation effective April 1, 1986, and offsets the price reductions that the Corporation was forced to make in early 1987.

During the year, the Corporation intervened in the hearing before the National Energy Board in respect of an application by Westcoast for the setting of new tolls for the transportation of natural gas to domestic and export markets for each of the years 1987 and 1988. On December 10, 1987, the Board released its Reasons for Decision which established Westcoast's total revenue requirement for each of these years.

The Board accepted, for toll design purposes, the contract demand levels in the relevant domestic sales and service contracts and, in respect of export sales, the lower contract demand levels as set out in the amended Westcoast/NWP sales agreement effective November 1, 1987. As a result of the new tolls being lower than the interim tolls charged since January 1, 1987, pending the decision of the Board, Westcoast rebated to the Corporation an amount of $16,664,335, which represented the excess cost-of-service recovered in 1987 together with carrying charges. This amount, together with interest thereon, was included in the Natural Gas Price Adjustment Fund balance at March 31, 1988, and subsequently rebated to producers after the end of the fiscal year.

The fiscal year under review was notable for the dramatic improvement in the operating results of the methanol plant at Kitimat, B.C. which is currently operated by Ocelot Ammonia Company on behalf of Ocelot Investments Ltd. ("Investments"). This financial improvement was due to the operating efficiencies undertaken in late 1986 and early 1987, the successful marketing of the methanol production and the increase throughout the year in the world price of methanol. Both the methanol plant and the ammonia plant, which is located on land adjacent to the former, have operated during the year in excess of their respective design capacities.

During 1987, no payment was made by Investments to reduce the indebtedness of that company for unpaid fuel and feedstock gas and the repayment obligations under the debenture agreement with British Columbia Gas Corporation. However, in 1988, as a consequence of the improved operating results of the methanol plant, referred to above, payments have been received by the Corporation reducing the indebtedness outstanding under the debenture agreement. It is anticipated that further payments will be received, which will eliminate the amount owing for gas delivered and will reduce, considerably, the indebtedness owing to the Corporation under the debenture. It is expected that all amounts owed by Investments to the Corporation will be recovered in full.

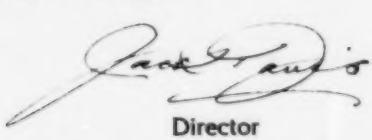
NATURAL GAS PRICE ADJUSTMENT FUND

Balance Sheet

March 31, 1988

	1988	1987
ASSETS		
Cash	$ 47,730,438	$ 38,677,317
Accounts receivable	39,277,483	47,879,455
Prepaid expenses	8,153	3,977
	$ 87,016,074	$ 86,560,749
LIABILITIES		
Accounts payable and accrued charges	$ 37,963,262	$ 45,778,993
Amount available for distribution (Note 2)	49,052,812	40,781,756
	$ 87,016,074	$ 86,560,749

Approved by the Directors



Director

Director

See accompanying notes to financial statements.

NATURAL GAS PRICE ADJUSTMENT FUND

Statement of Revenue, Expenditure and Fund Balance

Year Ended March 31, 1988

	1988	1987
Revenue		
Sales from natural gas, natural gas liquids and sulphur (Note 2)	$397,953,897	$397,974,979
Interest	2,122,038	2,414,354
	$400,075,935	$400,389,333
Expenditure		
Natural gas purchases	352,675,110	369,803,152
Price adjustments	18,590,888	18,004,446
Payments for natural gas liquids	18,462,547	10,372,994
Administrative and general expenses	2,076,334	1,832,904
	391,804,879	400,013,496
Excess of revenue over expenditure	8,271,056	375,837
Fund balance at beginning of year, as restated (Note 3)	40,781,756	40,405,919
Fund balance at end of year	$ 49,052,812	$ 40,781,756

See accompanying notes to financial statements.

NATURAL GAS PRICE ADJUSTMENT FUND

Notes to the Financial Statements

March 31, 1988

Note 1 — Statutory Requirements

The Natural Gas Price Adjustment Fund is established by the Natural Gas Price Act, 1985.

Note 2 — Significant Accounting Policies

GAS SALES

Under the terms of an agreement between Westcoast Energy Inc. and British Columbia Petroleum Corporation effective November 1, 1973, the Corporation sells natural gas to Westcoast at a price equal to the gross revenue received by that Company on the resale thereof less that Company's cost of service, in respect of gathering, processing and transporting the gas, for the month in which such resale takes place. The revenue from sales of natural gas is paid into the Natural Gas Price Adjustment Fund for subsequent distribution to producers, as required by the Natural Gas Price Act.

CHANGES IN FINANCIAL POSITION

A statement of changes in financial position is not provided as disclosure of such information in these financial statements is considered to be adequate.

Note 3 — Prior Year Adjustment

By an order dated November 9, 1987, the National Energy Board instructed Westcoast Energy Inc. to make certain amendments to its tariffs and tolls, the net effect of which was to increase the revenue of the fund in the year ended March 31, 1987. As a result of this order, the fund balance at that date, previously reported as $38,492,214, has been restated to reflect this increase in revenue amounting to $2,289,542.

Auditors' Report

To the Lieutenant-Governor in Council, Province of British Columbia:

We have examined the balance sheet of the Natural Gas Price Adjustment Fund as at March 31, 1988, and the statement of revenue, expenditure and fund balance for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the Fund as at March 31, 1988, and the results of its operations for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Wolrige Mahon

Wolrige Mahon
Chartered Accountants

Vancouver, B.C., June 1, 1988

PETROLEUM CORPORATION FUND

Balance Sheet

March 31, 1988

	1988	1987
ASSETS		
Current assets		
Cash	$ 7,143,864	$ 31,496,926
Accounts receivable	8,748,216	4,596,339
	15,892,080	36,093,265
Prepaid gas (Note 3)	33,125,554	40,238,705
Property account (Note 4)	123,596	178,789
Other assets		
Deferred receivable (Note 5)	53,240,797	48,023,965
Debt issue expenses	—	42,420
	53,240,797	48,066,385
	$ 102,382,027	$ 124,577,144
LIABILITIES		
Current liabilities		
Accounts payable and accrued charges	$ 5,885,302	$ 2,907,619
Deferred liability due within one year (Note 6)	1,000,000	1,000,000
Long-term debt due within one year	—	30,000,000
	6,885,302	33,907,619
Deferred liability (Note 6)	2,083,333	3,083,333
Surplus	93,413,392	87,586,192
	$ 102,382,027	$ 124,577,144

Commitments (Note 8)

Approved by the Directors

Director

Director

See accompanying notes to financial statements.

PETROLEUM CORPORATION FUND

Statement of Revenue, Expenditure and Surplus

Year Ended March 31, 1988

	1988	1987
Revenue		
Interest (Note 7)	$ 3,985,694	$ 3,778,444
Miscellaneous income	106,080	104,640
Gain (loss) on prepaid gas (Note 3)	1,834,023	(3,346,914)
Gain (loss) on disposal of assets	11,700	(415)
	5,937,497	535,755
Expenditure		
Administrative and general expenses	110,297	309,917
Net income	5,827,200	225,838
Surplus at beginning of year	87,586,192	102,360,354
	93,413,392	102,586,192
Deduct: Transfers to Provincial Treasury	—	15,000,000
Surplus at end of year	$ 93,413,392	$ 87,586,192

See accompanying notes to financial statements.

PETROLEUM CORPORATION FUND

Statement of Changes in Financial Position

Year Ended March 31, 1988

	1988	1987
Operating activities		
Operations		
Net income	$ 5,827,200	$ 225,838
Add items not involving a flow of cash:		
— Depreciation and amortization	148,500	147,060
— Loss (gain) on disposal of fixed assets	(11,700)	415
Cash from operations	5,964,000	373,313
Recovery of prepaid gas	7,113,151	14,007,860
Transfers to Provincial Treasury	—	(15,000,000)
	13,077,151	(618,827)
Financing activities		
Mortgages	—	63,980
Increase (decrease) in deferred liability	(1,000,000)	(916,667)
Repayment of long-term debt	(30,000,000)	—
	(31,000,000)	(852,687)
Investing activities		
Property additions	(50,887)	(15,987)
Proceeds from sale of fixed assets	11,700	1,710
Increase in deferred receivable	(5,216,832)	(3,023,965)
	(5,256,019)	(3,038,242)
Changes in non-cash working capital		
Accounts receivable	(4,151,877)	1,556,431
Accounts payable and accrued charges	2,977,683	1,783,222
	(1,174,194)	3,339,653
Increase (decrease) in cash position during the year	(24,353,062)	(1,170,103)
Cash position at beginning of year	31,496,926	32,667,029
Cash position at end of year	$ 7,143,864	$ 31,496,926

See accompanying notes to financial statements.

PETROLEUM CORPORATION FUND

Notes to the Financial Statements

March 31, 1988

Note 1 — Statutory Requirements

The Petroleum Corporation Fund is established by the Petroleum Corporation Act.

Note 2 — Significant Accounting Policies

CONSOLIDATION

The Petroleum Corporation Fund financial statements include the accounts of the Corporation's subsidiary, British Columbia Gas Corporation.

GAS SALES

Under the terms of an agreement between Westcoast Energy Inc. and British Columbia Petroleum Corporation effective November 1, 1973, the Corporation sells natural gas to Westcoast at a price equal to the gross revenue received by that Company on the resale thereof less that Company's cost of service, in respect of gathering, processing and transporting the gas, for the month in which such resale takes place. Prior to July 1, 1985, revenue from sales of natural gas was paid into the Petroleum Corporation Fund. Effective July 1, 1985, the revenue from such sales is paid into the Natural Gas Price Adjustment Fund, as required by the Natural Gas Price Act, 1985.

DEPRECIATION

Furniture, equipment, automobiles and leasehold improvements are recorded at cost and depreciation is provided at rates considered adequate to amortize the cost over the service lives of the assets. Depreciation is computed on a straight-line basis.

Note 3 — Prepaid Gas

Under its gas purchase contracts with producers, the Corporation is obligated to purchase and take delivery of, or pay for, a specified minimum annual volume of gas. In the contract years 1980-1987 inclusive, the Corporation was unable to take delivery of the minimum volume of gas and, therefore, is liable to pay for the resulting shortfall (deficiency gas). The Corporation is entitled to take delivery of deficiency gas within a period of ten years from the date incurred, with an adjustment for any increase in the prices prevailing when such gas is delivered.

Prepaid gas outstanding at March 31, 1988, has been calculated at the lower of cost or current value.

Note 4 — Property Account

	Cost	Accumulated Depreciation & Amortization	1988 Net Book Value	1987 Net Book Value
Furniture	$403,014	$348,696	$ 54,318	$111,076
Automobiles	48,947	11,703	37,244	10,599
Leasehold Improvements	250,538	218,504	32,034	57,114
	$702,499	$578,903	$123,596	$178,789

Note 5 — Deferred Receivable

The deferred receivable of $53,240,797 represents the amount of credit extended to Ocelot Investments Ltd. as at March 31, 1988, under an agreement with the Corporation and its subsidiary, British Columbia Gas Corporation. Of this receivable, which is secured by a first fixed and floating charge on the assets of that company, an amount of $35,740,741 is repayable by way of equal monthly instalments to April 1, 2004, with interest at three quarters of one percent over prime, and an amount of $3,083,333 is repayable by way of equal monthly instalments to April 1, 1991, at the same interest rate. The balance of the deferred receivable, amounting to $14,416,723, represents unpaid obligations of Ocelot Investments Ltd. under this agreement and other contracts, including accrued interest thereon.

No provision has been made in these financial statements for the possible non-recovery of this receivable as the value of the secured assets is considered adequate to repay the amounts owing.

Note 6 — Deferred Liability

The deferred liability of $3,083,333 represents the deferral, under an agreement with Pacific Northern Gas Ltd., in the payment of a portion of the billing for gas delivered to British Columbia Gas Corporation. This amount, including accrued interest at a rate of not less than three quarters of one percent over prime, is repayable over a period of five years which commenced May 1, 1986.

Note 7 — Interest

	1988	1987
Interest Income		
Province of British Columbia	$2,295,961	$2,705,856
Other	5,144,653	4,527,508
	7,440,614	7,233,364
Less: Interest expense	3,412,500	3,412,500
Amortization of debt issue expenses	42,420	42,420
	3,454,920	3,454,920
	$3,985,694	$3,778,444

Note 8 — Commitments

(1) Under agreements with producers which waived the Corporation's liability to pay for deficiency gas incurred in 1980, the Corporation is committed to purchase and take delivery of, or pay for, a specified volume of such gas in each year to 1991. At March 31, 1988, the Corporation's aggregate liability under these agreements was estimated at approximately $2,324,000.

(2) The Corporation has commitments under agreements for the lease of office premises extending to 1989. The aggregate rentals payable under leases amounted to approximately $352,000 at March 31, 1988.

Note 9 — Comparative Figures

Certain comparative figures have been reclassified to conform to the 1988 presentation.

Auditors' Report

To the Lieutenant-Governor in Council, Province of British Columbia:

We have examined the balance sheet of the Petroleum Corporation Fund as at March 31, 1988, and the statements of revenue, expenditure and surplus and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the Fund as at March 31, 1988, and the results of its operations and the changes in its financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Wolrige Mahon

Wolrige Mahon
Chartered Accountants

Vancouver, B.C., June 1, 1988

Five Year Summary

YEAR ENDED MARCH 31	1988	1987	1986	1985	1984
Volumes					
Domestic sales - (10^3m^3)	**3,822,342**	4,146,107	4,948,419	4,894,318	4,403,010
- (Mcf)	**134,932,341**	146,361,570	174,683,961	172,774,147	155,430,488
Export sales - (10^3m^3)	**2,528,064**	2,495,983	1,771,653	1,886,415	2,038,496
- (Mcf)	**89,243,085**	88,110,615	62,541,041	66,592,275	71,960,884
Sulphur sales - tonnes shipped	**308,645**	276,690	239,521	265,482	282,449
Natural gas liquids - (m^3)	**253,069**	231,127	191,365	227,665	231,469
Average Selling Price of Gas					
Domestic - $ per 10^3m^3	**82.7464**	89.8580	99.6192	92.2243	81.4546
- $ per Mcf	**2.3440**	2.5455	2.8220	2.6125	2.3074
Export - $ per 10^3m^3	**94.8111**	86.8049	150.4764	159.9602	198.6800
- $ per Mcf	**2.6858**	2.4590	4.2627	4.5313	5.6282
Average Regulated Selling Price					
- $ per 10^3m	**48.4609**	55.5597	70.4299	—	—
- $ per Mcf	**1.4003**	1.6054	2.0351	—	—
Average Purchase Price of Gas					
Old gas - $ per 10^3m^3	—	—	—	55.4341	57.2490
- $ per Mcf	—	—	—	1.6018	1.6542
New gas - $ per 10^3m^3	—	—	—	62.3398	64.9556
- $ per Mcf	—	—	—	1.8013	1.8769

Corporate Information

Directors:

Honourable Jack Davis
Minister of Energy, Mines & Petroleum Resources
Chairman of the Board

John P. Crone
Businessman
Victoria, B.C.

Larry E. Fisher
Businessman
Surrey, B.C.

Hon. Audrey L. Moore
Mayor of Castlegar, B.C.

Donald W. Rawlyk
General Manager & Manager, Natural Gas Division

Senior Personnel:

Donald W. Rawlyk
General Manager & Manager, Natural Gas Division

Sidney T. Akers
Manager, Gas Supply & Special Projects

Gordon S. Thomas
Comptroller

Bruna M. Martinuzzi
Corporate Secretary

Leonard D. Anderson
Chief Geologist

J. Brian Williston
Chief Engineer

Neil C. Beaton
Administrator, Gas Proration

Gordon A. Pearson
Assistant Comptroller

Corporate Offices:

1199 West Hastings Street
6th Floor
Vancouver, B.C. V6E 3T5
Telephone (604) 661-3300
Fax (604) 661-3324
Telex 04-54530

Legal Advisors:

Davis & Company
2800 Park Place
666 Burrard Street
Vancouver, B.C. V6C 2Z7

Auditors:

Wolrige, Mahon
9th Floor
400 Burrard Street
Vancouver, B.C. V6C 3B7